

Message Text

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ACTION EB-08

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P 110926Z FEB 77
FM AMEMBASSY MANILA
TO SECSTATE WASHDC PRIORITY 5954

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PASS: USDA

E O 11652: GDS
TAGS: ETRD, EAGR, RP
SUBJ: SUGAR: GOP NEGOTIATIONS WITH U.S. COMPANIES

REF: A. MANILA 1461; B. STATE 24939; C. MANILA 2010

SUMMARY: NEGOTIATIONS CONTINUE ON NEW PARTICIPATING CONTRACT BETWEEN SUCREST AND GOP. DRAFT CONTRACT REPORTEDLY PRO-VIDES FOR PRICE OF 12 CENTS PER POUND, SALE OF MINIMUM OF 700,000 TONS PER YEAR, AND SUCREST ADVANCE LOAN ON SUGAR WHEN PRODUCED. SUCREST REPS CLAIM TRADING IN SUCREST STOCK WILL BE RESUMED FEB. 14. END SUMMARY

1. GOP SOURCES AND SUCREST OFFICIALS HAVE PROVIDED SOME ADDITIONAL INFORMATION REGARDING ONGOING GOP-SUCREST RENEGOTIATION OF PARTICIPATING SUGAR CONTRACT. AS REPORTED REF. C, TALKS BETWEEN SUCREST AND GOP REPS (LED BY PANFILO DOMINGO, PRESIDENT OF PHILIPPINE NATIONAL BANK) HAVE BEEN UNDER WAY IN MANILA SINCE JAN. 17. SUCREST TEAM IS HEADED BY ALLERTON D. MARSHALL, VICE PRESIDENT AND TREASURER, AND INCLUDES PETER A. MEYER, VICE PRESIDENT, AND RICHARD S. SAVITT, A LAWYER WITH STROOCK & STROOCK LAVAN, NEW YORK.

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2. MARSHALL IS GENERALLY SATISFIED WITH PACE OF TALKS, ALTHOUGH HE SAYS LAST FEW DAYS HAVE BEEN DIFFICULT DUE TO COMPLEXITY OF FINANCIAL ARRANGEMENTS IN CONTRACT. WHILE NEITHER SIDE IS FREE WITH DETAILS, EMBASSY UNDER-STANDS CONTRACT IS BEING DRAWN UP ALONG FOLLOWING LINES: THE CONTRACT CITES A PRICE OF 12 CENTS PER POUND AND WILL PROVIDE FOR SALE OF A MINIMUM OF 700,000

TONS OF SUGAR PER YEAR. IN ADDITION, THE CONTRACT WILL CONTAIN A SO-CALLED "RED CLAUSE" WHICH PROVIDES THAT SUCREST WILL MAKE AN ADVANCE LOAN ON THE SUGAR WHEN IT IS PRODUCED. THE LOAN WILL BE MADE ON THE BASIS OF "QUEDANS", WAREHOUSE RECEIPTS ISSUED BY THE MILL, AT 12-CENT PRICE, WITH GOP RETAINING TITLE TO SUGAR.

FILIPINOS HAVE INSISTED ON 12 CENT PRICE, CLAIMING THAT THIS FIGURE REPRESENTS AVERAGE PRODUCTION COST IN THE PHILIPPINES. (EMBASSY DOES NOT RPT NOT BELIEVE AVERAGE PRODUCTION COST CAN BE MUCH HIGHER THAN 10 CENTS PER POUND AND IT MAY BE CONSIDERABLY LOWER. THE PRICE PAID BY PHILEX (COMPOSITE PRICE) IS NOW 7.9 U.S. CENTS PER POUND.)

ACTUAL COST OF SUGAR TO SUCREST WILL, HOWEVER, BE DETERMINED AT SOME POINT AFTER SUGAR HAS BEEN SHIPPED AND ADVANCE PAID BY SUCREST WILL BE ADJUSTED TO REFLECT WORLD MARKET PRICE. GOP SOURCES ADDED THAT AS LONG AS PRICE OF SUGAR IS BELOW 12 CENTS, CONTRACT PROVIDES THAT SUCREST WILL RECOVER REFINING COSTS AND SOME OTHER UNSPECIFIED FINANCIAL COSTS, BUT NO "PROFITS". IN RETURN, SUCREST'S PROFITS WILL INCREASE DISPROPORTINATELY IF PRICE RISES ABOVE 12 CENTS. WHILE THIS FORMULATION IS VAGUE, IT DOES SEEM TO INDICATE THAT GOP HAS SUCCEEDED, OR IS ABOUT TO SUCCEED, IN INCREASING ITS SHARE OF THE RETURNS ON SUGAR SOLD FOR UNDER 12 CENTS PER POUND.

4. SUCREST TEAM WAS AWARE OF RUMORS THAT THEIR COMPANY WAS HAVING DIFFICULTY ARRANGING NECESSARY FINANCING TO MEET GOP REQUEST FOR LOANS UNDER NEW CONTRACT. MARSHALL CONFIDENTIAL

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STATED EMPHATICALLY THAT THIS WAS NOT TRUE, AND NOTED THAT TRADING IN SUCREST STOCK WOULD BE RESUMED ON MONDAY, FEB. 14. SUCREST IS ARRANGING BANK GUARANTEES TO SPREAD RISK INHERANT IN THE LOANS, BUT IMPLIED THAT THESE GUARANTEES HAD ALREADY BEEN OBTAINED FROM U.S. BANKS.

5. SUCREST REPS CONFIRMED ALL THREE RUMORS WHICH EMBASSY HAD HEARD REGARDING SUSPENSION OF TRADING IN SUCREST STOCK: (1) PUBLIC ACCOUNTING FIRM AUDITING SUCREST WAS SUSPICIOUS THAT KICK-BACKS HAD BEEN MADE IN CONNECTION WITH PARTICIPATING CONTRACT WITH THE PHILIPPINES. (2) IN ADDITION, ACCOUNTING FIRM WOULD NOT ACCEPT INVENTORY

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EVALUATION PRACTICES FOLLOWED BY SUCREST. (3) FINALLY, THE SEC CLAIMED THAT BRIEF DESCRIPTION OF THE PHILIPPINE CONTRACT IN SUCREST'S FORM 10-4 DID NOT RPT NOT MEET RULES OF DISCLOSURE. MARSHALL SAYS THAT THE AUDITORS ARE NOW SATISFIED THAT NO KICK-BACKS WERE MADE. THE INVENTORY EVALUATION PROBLEMS WERE RESOLVED WHEN SUCREST AGREED TO IMPLEMENT A PACKAGE OF MANAGEMENT REFORMS WHICH INCLUDED REPLACING THE PRESIDENT OF THE COMPANY. THE DISPUTE WITH THE SEC WAS RESOLVED BY SUBMITTING A COMPLETE DESCRIPTION OF THE PARTICIPATING CONTRACT IN A CONFIDENTIAL FORM 10-4.

6. AS DISCUSSED REF. C, SUCREST HAS NOT RPT NOT, IN FACT, PAID FOR LAST TWO SHIPMENTS OF SUGAR FROM THE PHILIPPINES. HOWEVER, SUCREST CLAIMS THAT THEY ARE WITHHOLDING PAYMENT IN CONNECTION WITH 35 MILLION DOLLARS WHICH PHILIPPINES OWES SUCREST AS A RESULT OF ADVANCE PAYMENT OR LOAN PROVISIONS IN CURRENT PARTICIPATING CONTRACT. SUCREST REPS DOWNPLAY SERIOUSNESS OF THIS DISPUTE, QUALIFYING IT AS PART OF CURRENT NEGOTIATING PROCESS.

7. COMMENT: AS DISCUSSED IN PARA 3 OF REF. C, THE GOP SUGAR MARKETING MECHANISM BADLY NEEDS CASH, AND THE INCLUSION OF A LOAN PROVISION IN THE RENEGOTIATED PARTICIPATORY CONTRACTS COULD SOLVE THIS PROBLEM

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WITHOUT INCREASING GOP'S EXTERNAL DEBT. EVEN MORE INTERESTING IS TACTIC OF CITING A PURPORTED COST OF PRODUCTION, AND WRITING THE CONTRACT IN SUCH A WAY THAT THE PURCHASING REFINERY CAN DO LITTLE MORE THAN COVER COSTS WHEN SUGAR FALLS BELOW THE UNILATERALLY DECLARED "COST OF

PRODUCTION", EMBASSY HAS BEEN TOLD THAT GOP USED THIS SAME APPROACH IN 700,000 TON SALE TO PHILLIP BROTHERS (REF. A), AND SUCREST REPS SPECULAT THAT PHILLIP BROTHERS SALE IS A CONTINGENT SALE WHICH IS DESIGNED TO PUT PRESSURE ON SUCREST AND WHICH WILL ONLY TAKE EFFECT IF SUCREST CONTRACT IS NOT RPT NOT RENEGOTIATED.

8. WITH REGARD TO INTERNATIONAL COMMODITY MARKETING PRACTICES, THE MOST INTERRESTING ASPECT OF THE NEW PARTICIPATING CONTRACT, AS WE NOW UNDERSTAND IT, IS THE INCLUSION OF CONCEPT OF AVERAGE COST OF PRODUCTION. EMBASSY BELIEVES THAT KEY ELEMENT OF GOP SUGAR POLICY IS PRESIDENT MARCOS' ACUTE FRUSTRATION THAT HE CANNOT CONTROL THE MARKETING ABROAD OF HIS PRIMARY EXPORT COMMODITY, SUGAR, AND THAT THIS FRUSTRATION IS REFLECTED IN THE STRUCTURE OF THE PROPOSED PARTICIPATING CONTRACT. THE NEW CONTRACT CAN ALSO BE VIEWED IN A LARGER CONTEXT AS PART OF THE CONTINUING EFFORT OF LDC'S TO REORGANIZE CURRENT ECONOMIC ORDER TO TAKE FULLER ACCOUNT OF THEIR PRODUCTION COSTS (AS THEY SEE THEM) AND TO INSURE LDC'S A LARGER SHARE OF PROCESSING INDUSTRY PROFITS.

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